

# Bob Brinker's Markettimer

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"Don't let the present overwhelm  
your sense of the possibilities  
of the future."

... Timothy Forbes

## STOCK MARKET TIMING

DJIA: 8663.50

S & P 500: 916.07

During the secular bear market that began February 9, 1966 and continued through August 12, 1982, there were four major cyclical bear market bottoms recorded by the Standard and Poor's 500 Index.

<u>Bottom</u>	<u>Trailing P/E</u>	<u>Magnitude of Next Advance</u>	<u>Duration</u>
Oct. 7, 1966	13.4	32.4%	26 months
May 6, 1970	13.6	66.4%	32 months
Oct. 3, 1974	7.3	75.9%	21 months
Aug. 12, 1982	7.3	65.0%	15 months

We focus our attention on the first three of these cyclical bear market bottoms, because they occurred within an ongoing secular bear market. Although the August 12, 1982 bottom was the lowpoint for the final cyclical bear market of the 1966–1982 secular bear trend, it also marked the starting point for a new secular bull market, which we do not consider a possibility in the current situation. In our view, the probability of a new secular bull market beginning anytime soon is essentially zero, given the fact we are only in the third year of the current secular bear megatrend.

Based on this analysis, we view the three cyclical bear market bottoms that occurred within the 1966–1982 secular bear market as most relevant to the current market experience. As subscribers know, we believe the current secular bear market began in the first quarter of year 2000. Therefore, any bear market bottoms that occur going forward for many years are expected to be cyclical bear market bottoms within an ongoing secular bear trend, as was the case with the first three bottoms listed above.

For secular megatrend skeptics, consider the fact that the Standard and Poor's 500 Index reached its record closing high of 1527.46 in March of 2000. Now, nearly 30 months later, the index stands far below that level with no likelihood of achieving significant new record highs anytime soon based on any reasonable assessment of corporate earnings potential.

Despite the difficulty the Standard and Poor's 500 Index will have in reaching new record highs, we believe the ongoing secular megatrend we are now experiencing will see a succession of cyclical bull and bear markets lasting approximately one-to-three years each. In our view, the cyclical bull market periods offer the potential to generate stock market gains for those savvy enough to invest their stock market cash reserves at the right time. However, this strategy will also involve raising stock market cash reserves in the vicinity of cyclical bull market highs, since cyclical bear markets are expected to follow cyclical bull markets with the overall market as measured by the Standard and Poor's 500 Index making no major progress beyond the record high recorded in March of year 2000.

Reviewing the cyclical bull markets that occurred within the February 1966 to August 1982 secular bear megatrend, the gains ranged from 32.4% to 75.9%, for a median advance of 54.2%. In all cases, the duration was within a range of one-to-three years.

Regarding valuation, we do not believe it is absolutely necessary for the trailing price/earnings ratio to return to the 7.3 to 13.6 range that prevailed at all of the cyclical bear market bottoms during the 1966-1982 secular bear market. However, current market valuations remain extended based on historical comparison, regardless of which numbers are used. Here is a look at valuation comparisons we consider relevant:

<u>Date</u>	<u>Price/Earnings Ratio</u>	<u>Comment</u>
Oct. 7, 1966	13.4	cyclical bear market bottom
May 6, 1970	13.6	cyclical bear market bottom
Oct. 3, 1974	7.3	cyclical bear market bottom
Aug. 12, 1982	7.3	cyclical bear market bottom and secular bear market bottom
July 23, 2002(low-to-date)	23.9	based on 2001 operating earnings
July 23, 2002(low-to-date)	18.9	based on 2002 est. oper. earnings
July 23, 2002(low-to-date)	21.5	* based on 2002 est. GAAP earnings
Sept. 2, 2002	27.4	based on 2001 operating earnings
Sept. 2, 2002	21.7	based on 2002 est. oper. earnings
Sept. 2, 2002	24.7	* based on 2002 est. GAAP earnings

\* GAAP earnings are based on generally accepted accounting principles and include all charges except those from discontinued operations and some extraordinary items.

These valuation comparisons are especially relevant within the context of the current **Marketimer** economic outlook. We anticipate real gross domestic product growth for calendar year 2002 will be within a range of 2% to 2.5%. So far, for the first-half of the year, the number is running at a 3% annual rate. However, this number has been helped by the large reduction in inventory levels that pushed the first quarter growth rate to 5%. The second quarter growth rate receded to 1.1%.

Nothing has happened during the last month to change our economic and corporate earnings forecast. We continue to estimate Standard and Poor's 500 Index operating earnings for calendar year 2002 of \$42.20, well below Wall Street expectations. Our calendar year 2003 operating earnings estimate remains at \$47.10, also well below Wall Street forecasts. Our GAAP estimates for 2002 and 2003 are \$37.20 and \$42.10.

We believe many corporations will take earnings haircuts going forward as over-optimistic pension fund return assumptions come back to reality. Also, we believe the tendency of corporate chieftains to write-off operating losses as expenses will come under increased scrutiny from the chastened accounting profession, which will have the effect of further restraining corporate earnings growth.

Recent disclosures of corporate malfeasance have surely damaged investor confidence. We find ourselves in agreement with Wall Street sage Peter Bernstein, author of **Against The Gods, The Remarkable Story of Risk**, who recently observed "The magnificent achievements of the American economy from the end of 1978 to the mid-1990's have been besmirched by the greed of malefactors who spat upon the altar of maximizing shareholder value. As a result, many of the accomplishments of the past twenty years are now in danger of being discarded or distorted beyond recognition."

In our view, the economy remains in a state of suspended animation. The Federal Reserve has been "pushing on a string" as they have driven the real cost of short-term money to the zero level. However, with the exception of mortgage lending, borrowers remain reluctant to increase their debt loads. Corporate chieftains are more interested in conserving their financial resources than embarking on risky new endeavors. There is very little reason for companies to adopt aggressive business plans that involve new plant and equipment. Furthermore, the labor situation remains tenuous with job growth anemic so far in 2002.

Investors have remained transfixed on "missing the bottom" even though several previous "bottoms" proclaimed by Wall Street gurus have been without substance. **Marketimer** remains focused on working to identify a true cyclical bear market bottom that has the potential to open the door to a sustainable uptrend with major potential over a period of one-to-three years. In our view, more patience will be needed to get through this difficult stock market period. However, this cyclical bear market is getting older, and eventually conditions will change. We continue to believe that a new cyclical bull market buy signal will develop either later this year or during the first-half of 2003.

We are maintaining our hold rating on Nasdaq 100 (QQQ) shares in anticipation of much higher prices for the shares in the next cyclical bull market. We also continue to recommend holding stock market cash reserves until our long-term stock market timing model returns to a fully invested position. Subscribers may visit our website at [www.bobbrinker.com](http://www.bobbrinker.com) to check the bulletin page on a regular basis as any major change in our recommendations will appear there first if the change occurs between monthly newsletter editions. Also, when our next buy signal occurs, we will post our model portfolio recommendations for models one, two, three and active/passive for subscribers at the website in addition to mailing the information.

#### FEDERAL RESERVE UPDATE

The Federal Reserve remains accommodative. The monetary base shows real year-over-year growth of 7.6%, versus 10.3% last month. The growth of M-1, which consists primarily of currency in circulation and demand deposits, has been disappointing. M-1 has risen only 2.1% in real terms year-over-year, down from 3.7% last month. The broader M-2 monetary aggregate shows real year-over-year growth of 6%, the same percentage change recorded last month.

**Table A**  
Latest Monthly Data  
(Billions)

	<u>August 2002</u>	<u>August 2001</u>	<u>Y-O-Y</u> <u>Changes</u>	<u>Real Y-O-Y*</u> <u>Changes</u>
Monetary Base	\$ 686.4	\$ 629.4	+ 9.1%	+ 7.6%
M-1	\$ 1,183.9	\$ 1,142.5	+ 3.6%	+ 2.1%
M-2	\$ 5,686.4	\$ 5,287.8	+ 7.5%	+ 6.0%

\* Real changes year-over-year, adjusted for consumer price index increase of 1.5% for the 12-month period through 7-31-02.

The Federal Open Market Committee left rates unchanged at their August meeting, however they changed the bias statement to reflect their perception that there is risk of further economic weakness going forward. Short-term rates remain at 40-year lows, with the federal funds rate at 1.75% and the discount rate at 1.25%. Adjusted for inflation, short-term rates are essentially at the zero level.

BOB BRINKER'S RECOMMENDED LIST OF NO-LOAD FUNDS

FUND	INV.*	SIZE	% Total Return						\$1000 INV. 1-1-97=	EST. <sup>a</sup>	TEL.	ANN. <sup>b</sup>	PRICE
	OBJ.	MIL.\$	'97	'98	'99	'00	'01	'02 (8-31)		YD.	SWCH	EXP.	8-31-02
Baron Growth Fund 767 Fifth Avenue 49 <sup>th</sup> Floor New York, NY 10153 800-992-2766	G BGRFX	\$ 856	31.1	0.1	44.7	(4.6)	12.7	(8.2)	\$ 1874	0.0%	#	1.40%	28.17
Baron Small Cap Fund 767 Fifth Avenue 49 <sup>th</sup> Floor New York, NY 10153 800-992-2766	CGA BSCFX	\$ 710	-	2.2	70.8	(17.5)	5.2	(6.8)	---	0.0%	#	1.39%	14.17
Gabelli Asset Fund One Corporate Center Rye, NY 10580 800-422-3554	G GABAX	\$ 1668	38.1	15.9	28.5	(2.4)	0.2	(13.9)	\$ 1732	0.0%	Yes	1.37%	28.39
TIAA/CREF Equity Index 730 Third Avenue New York, NY 10017 800-223-1200	Russell 3000 TCEIX	\$ 116	-	-	-	-	(11.6)	(18.8)	---	1.0%	Yes	0.26%	6.54
TIAA/CREF Growth&Income 730 Third Avenue New York, NY 10017 800-223-1200	G&I TIGIX	\$ 514	-	30.5	24.5	(7.3)	(13.4)	(20.9)	---	1.0%	Yes	0.43%	9.50

\* Investment Objective Codes: CGA = Capital Gains Aggressive; G = Growth; G&I = Growth & Income

a) Estimated annual yield represents approximate investment income for last 12-months expressed as percentage of fund assets.

b) Annual expense ratio reflects investment advisory fees and other expenses expressed as percentage of total fund assets.

# Telephone redemption available.

**BOB BRINKER'S RECOMMENDED LIST OF NO-LOAD FUNDS**

FUND	INV. <sup>*</sup> OBJ.	SIZE MIL.\$	% Total Return						\$1000 INV. 1-1-97=	EST. <sup>a</sup> YD.	TEL. SWCH	ANN. <sup>b</sup> EXP.	PRICE 08-31-02
			'97	'98	'99	'00	'01	'02 (8-31)					
Dodge & Cox Stock 1 Sansome St. (35th Fl.) San Francisco, CA 94104 800-621-3979	G&I DODGX	\$ 11650	28.4	5.4	20.2	16.3	9.3	(8.2)	\$ 1898	1.7%	#	0.55%	91.45
Dodge & Cox Balanced 1 Sansome St. (35th Fl.) San Francisco, CA 94104 800-621-3979	G&I DODBX	\$ 7041	21.2	6.7	12.0	15.1	10.0	(3.0)	\$ 1779	3.1%	#	0.53%	62.46
Vanguard Calvert Social Index Fund P.O. Box 2600 Valley Forge, Pa 19482 800-662-2739	Social Index VCSIX	\$ 89	---	---	---	(9.0)	(14.1)	(22.4)	---	0.8%	Yes	0.25%	6.02
Schwab 1000 (R) 101 Montgomery St. San Francisco, CA 94101 800-266-5623	G SNXFX	\$ 3448	31.9	27.1	21.0	(8.2)	(12.3)	(18.5)	\$ 1331	1.1%	Yes	0.46%	26.05
Vanguard Index 500 P.O. Box 2600 Valley Forge, Pa 19482 800-662-2739	S&P 500 VFINX	\$ 58545	33.2	28.6	21.1	(9.1)	(12.0)	(19.3)	\$ 1339	1.5%	No	0.18%	84.83

Note: Neuberger & Berman Focus Fund has been deleted from coverage.

R) 0.50% redemption fee on shares held less than six months.

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BOB BRINKER'S RECOMMENDED LIST OF NO-LOAD FUNDS

FUND	INV.*	SIZE	% Total Return						\$1000 INV. 1-1-97=	EST. <sup>a</sup>	TEL.	ANN. <sup>b</sup>	PRICE
	OBJ.	MIL.\$	'97	'98	'99	'00	'01	'02 (8-31)		YD.	SWCH	EXP.	8-31-02
Vanguard Index (x) Extended Market Portfolio P.O. Box 2600 Valley Forge, Pa 19482 800-662-2739	Index VEXMX	\$ 2622	26.7	8.3	36.2	(15.5)	(9.2)	(16.9)	\$ 1192	1.1%	No	0.25%	19.19
Vanguard Index (x) Small Cap Stock Portfolio (address/phone above)	Russell 2000 NAESX	\$ 3032	24.6	(2.6)	23.1	(2.7)	3.1	(18.8)	\$ 1217	1.4%	No	0.24%	16.10
Vanguard Index Total Stock Market Portfolio (address/phone above)	Wilshire 5000 VTSMX	\$ 14077	31.0	23.3	23.8	(10.6)	(11.0)	(18.4)	\$ 1298	1.4%	No	0.20%	20.87
Vanguard International Growth Portfolio (address/phone above)	Non USA VWIGX	\$ 4970	4.1	16.9	26.3	(8.6)	(18.9)	(13.6)	\$ 984	1.8%	Yes	0.52%	12.97
Rowe Price European 100 East Pratt St. Baltimore, MD 21202 800-638-5660	Europe PRESX	\$ 704	17.0	25.8	19.7	(6.7)	(20.7)	(16.5)	\$ 1088	2.7%	Yes	1.01%	13.37
Longleaf Partner's Int'l 6410 Poplar Ave. Suite 900 Memphis, TN 38119 800-445-9469	Int'l Growth LLINX	\$ 907	---	---	24.4	25.9	10.5	(11.3)	---	1.1%	#	1.79%	10.95
Rydex OTC Fund 6116 Executive Blvd. Suite 400 Bethesda, MD 20852 800-820-0888	CGA RYOCX	\$ 661	21.9	86.5	100.6	(37.8)	(34.7)	(40.6)	\$ 1100	0.0%	Yes	1.15%	6.56

x) Vanguard Index Extended and Small Cap funds charge purchase fees of 0.5% or less to defray expenses of broad diversification;  
annual expense ratios on these funds are extraordinarily low.

#) telephone redemption available

## FEDERAL RESERVE UPDATE (continued from page 3)

The FOMC meets again September 24 and all signs point to continued economic stagnation, with little change in real GDP likely during the third quarter. This comes on the heels of second quarter real GDP growth of only 1.1%, and ongoing monthly new jobs figures that remain far below the 150,000 monthly average required to absorb new entries into the labor market. While it is possible the Fed will leave rates unchanged at the September 24 FOMC meeting, it is conceivable they could decide to reduce rates by 0.25% if they become more concerned about the direction the economy is taking. The recent change in the Federal Reserve's economic bias statement demonstrates that the economy has not responded to the eleven rate cuts implemented during 2001 despite the fact that Federal Reserve monetary policy has remained highly accommodative.

## INTEREST RATES / FIXED- INCOME SECURITIES

**Marketimer's** fixed-income recommendations have a current average yield of 4.67%, an average maturity of 4.3 years and an average duration of 2.9. Duration is the weighted average of the times that interest payments and the final return of principle are received. The academic rule of thumb is that the percentage change in the price of a bond or bond fund is the duration multiplied by the change in interest rates. Applying duration to the Vanguard Ginnie Mae Fund, the fund's current duration of 2.8 suggests that a one percent increase in corresponding interest rates would result in an estimated 2.8% decline in the fund's net asset value.

<u>Fund</u>	<u>Weighting</u>	<u>Yield</u>	<u>Avg. Mat.</u>	<u>Duration</u>
Vanguard Fixed-Income Short-Term Federal (VSGBX)	25%	2.85%	2.6	2.1
Vanguard Ginnie Mae Fund (800-662-7447)(VFIIX)	50%	5.09%	3.2	2.8
Dodge & Cox Income Fund (800-621-3979) (DODIX)	25%	5.64%	8.2	4.0

For subscribers who prefer to keep their fixed-income monies at Vanguard, a substitute for Dodge & Cox Income Fund is Vanguard Inflation Protection Securities Fund (VIPSX). This fund has a current base yield of 2.27%, plus inflation adjustments based on the consumer price index which are paid quarterly.

Our favorite money market funds are Vanguard Prime Money Market with a current yield of 1.53%, and for tax-exempt objectives, Vanguard Tax-Exempt Money Market, with a current yield of 1.31%. For tax-exempt investment income, we like state general obligation bonds with maturities in the 10-to-12 year range.

## ACTIVE/PASSIVE PORTFOLIO

This portfolio is designed for long-term no-load fund investment aimed at broad diversification, tax-efficiency, low-expenses and risk management. The portfolio currently holds 65% in stock market cash reserves, 25% in Vanguard Total Stock Market Index, 5% in T. Rowe Price European or Vanguard European Index, and 5% in Vanguard International Growth.

## INDIVIDUAL ISSUES

In order to limit specific stock risk, exposure to any one company stock should not exceed 4%. The following issues are currently rated hold:

<u>ISSUES</u>	<u>Beta</u>	<u>Exchange</u>	<u>Symbol</u>	<u>9-02 Price</u>	<u>Est. earnings per share</u>	
Microsoft	1.27	Nasdaq	MSFT	49.08	1.90 (6-03)	2.15 (6-04)
Vodafone/AirTouch	1.10	NYSE	VOD	16.00	0.81 (3-03)	0.84 (3-04)
S&P Dep. Receipts	1.00	AMEX	SPY	91.78	4.22 (2002)	4.71 (2003)
Total Market VIPERs	1.03	AMEX	VTI	85.71	n/a	
DJIA Diamonds	0.97	AMEX	DIA	86.52	4.95 (2002)	5.75 (2003)
Nasdaq 100 Index	1.67	AMEX	QQQ	23.49	*	

\* **Marketimer** estimates the forty-largest profitable companies in the Nasdaq 100 Index are trading at a weighted average multiple of 35.7 times projected 2002 earnings. These companies account for about 75% of the Nasdaq 100 Index capitalization.

## MARKETIMER NO-LOAD MUTUAL FUND MODEL PORTFOLIOS

The **Marketimer** no-load model portfolios are designed to provide investors seeking aggressive, growth and balanced objectives with a strategic approach to investing in no-load funds over the long-term.

Model Portfolio I is designed for investors with *aggressive growth* investment objectives. Such investors seek maximum returns and are willing and able to accept high levels of risk and volatility. Current income is not a factor in this portfolio.

Model Portfolio II is designed for investors with *long-term growth* objectives. Such investors seek to enhance the value of capital over time and assume a reasonable level of diversified market risk. Current income is not an important factor.

Model Portfolio III is designed as a *balanced* portfolio for current investment income along with capital preservation and modest growth. The portfolio is allocated evenly between equities and fixed-income securities. This portfolio is best suited to investors nearing or already enjoying a retirement lifestyle.

### MARKETIMER MODEL PORTFOLIO I

(\$20,000 value on 1-1-88)

<u>Current Holdings</u>	<u>Symbol</u>	<u>%</u>	<u>Beta</u>	<u>Value</u>	<u>8-31-02</u>	<u>% Change</u>
Baron Growth	BGRFX	05	1.00	\$	4,403	
Baron Small Cap.	BSCFX	05	1.05		3,630	
Rowe Price European	PRESX	05	0.69		2,424	
Vanguard Int'l. Growth	VWIGX	05	0.70		2,050	
TIAA/CREF Equity Index	TCEIX	15	1.02		13,544	
Money Market		<u>65</u>	<u>0.00</u>		<u>102,043</u>	
		<u>100%</u>	<u>0.33</u>	\$	<u>128,094</u>	<u>+ 540%</u>

### MARKETIMER MODEL PORTFOLIO II

(\$20,000 value on 1-1-88)

<u>Current Holdings</u>	<u>Symbol</u>	<u>%</u>	<u>Beta</u>	<u>Value</u>	<u>8-31-02</u>	<u>% Change</u>
Gabelli Asset Fund	GABAX	05	0.74	\$	3,668	
Rowe Price European	PRESX	05	0.69		2,705	
Dodge & Cox Stock Fund	DODGX	05	0.60		4,542	
Vanguard Int'l. Growth	VWIGX	05	0.70		2,083	
TIAA/CREF Equity Index	TCEIX	15	1.02		9,605	
Money Market		<u>65</u>	<u>0.00</u>		<u>82,474</u>	
		<u>100%</u>	<u>0.29</u>	\$	<u>105,077</u>	<u>+ 425%</u>

### MARKETIMER MODEL PORTFOLIO III

(\$40,000 value on 3-1-90)

<u>Current Holdings</u>	<u>Symbol</u>	<u>%</u>	<u>Beta</u>	<u>Value</u>	<u>8-31-02</u>	<u>% Change</u>
Vanguard Short-Term Federal	VSGBX	25	0.00	\$	29,103	
Vanguard Ginnie Mae Fund	VFIIX	25	0.00		33,283	
Rowe Price European	PRESX	02.5	0.69		2,104	
Dodge & Cox Stock Fund	DODGX	05	0.60		8,741	
TIAA/CREF Growth & Income	TIGIX	07.5	1.02		7,567	
Vanguard Int'l. Growth	VWIGX	02.5	0.70		1,797	
Money Market		<u>32.5</u>	<u>0.00</u>		<u>39,641</u>	
		<u>100%</u>	<u>0.14</u>	\$	<u>122,236</u>	<u>+ 206%</u>

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### HOW TO SUBSCRIBE TO **BOB BRINKER'S** MARKETIMER

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